GECO5105: Foundations of Political Economy II

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The Foundations of an Activist Fiscal Policy in the United States:

"The Great Engineer" and Public Works in the 1920s

Introduction and Methodology

In this paper we explore the development of the USA's use of public works as a macroeconomic (employment) stabilization tool. It is conventional wisdom that President Hoover was a "Do-Nothing President" in the face of the Great Depression when in fact his interest in fiscal policy and public works as an economic stabilization tool shows that this is not at all the case. Using contemporary academic and popular sources as well as economic histories of the period we trace the economic and political debates of the first use of public works by the federal government as a means for 'counter-cyclical' economic management.[1] In summary public works were part of the public debate immediately after the first World War, as a logical extension of the economic management tools used to fight that war.

[1] Reagan 2008 writes that "the forgotten depression of 1920-21 proved to be the sharpest economic downturn since the emergence of the business cycle in the early nineteenth century", page 3.

There were special interests, mostly labor unions, city planners and engineers, calling for a permanent works program at the federal level beginning after the war. This agitation, as well as perhaps his own interest in the subject, resulted in Herbert Hoover as Secretary of Commerce under President Warren Harding convening an "Unemployment Conference"[2] in 1921 during the Depression of 1920-21. It was not until the Great Crash of 1929 and the Great Depression which followed that public works spending at the federal level was seriously considered, and attempted, by the U.S. Government, under the Hoover Administration, in 1930. However by1931 due in part to a doubling of the US government's debt as a percentage of the economy during the four years of Hoover's administration, massive public works as an economic panacea were abandoned by Hoover and the idea of a federal public works program was shelved until the Roosevelt Administration's Works Progress Administration in 1935.

A Brief Summary of Some Findings on the Great Depression in Order to Place Employment Stabilization in Historical Context

What defines the Great Depression in the United States is not that the national output continually decreased for the duration (it did not), but that unemployment was abnormally high for the duration, averaging 17% for the period 1930-1940. This period was the first major economic downturn since the recession[3] of 1920-21, one from which the United States was able to quickly recovery relative to the rest of the world. Parker 2007 makes the case that it was viewed by

[2] Published as the *Report of the President's Conference on Unemployment* (1921), herewith known as the 1921 *Report* .

[3] It was called a 'depression' then, today we would call it a recession.

many economists at the time that the reason for the US's relative rapid recovery was due to successful interventionalist policies by the then relatively new (1913) central bank.[4] This perceived successful counter-cyclical monetary policy then helped to form a larger trend in economic thinking during the 1920s in which it was believed that the tools of modern economics and statistics could be used to 'stabilize' the economy against the harmful effects of the downward portion of the business cycle.[5] Fed policy was one driven towards price stability, it was assumed that this price stability would accommodate the money supply needs for trade (note there was no differentiating between the prices of consumption and investment goods in the aggregated notion of price stability) and would allow for a growth-oriented management of the economy.[6]

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[4] Parker also writes that in fact it was not monetary policy alone which allowed for the rapid recovery, but two additional factors. The first being that the US had a large export market due to the World War One-devastated Europe and the second being that the Gold Standard was not functioning (deflationary) due to the War Finance (fiat-backed, not species-backed, monies in those countries who fought the war) of WWI.

[5] In other words, *laissez faire* was over way before J.M. Keynes wrote "The End of Laissez Faire" in 1926.

[6] Rothbard 1975 uses Mises' theory of the trade cycle to show how this policy of price stability lead to an over-investment in long-term (durables) productive assets. As the manufacturing process for technologically-advanced goods became more efficient, prices should have gone down, not remained stable. This then led to overinvestment in more roundabout, capital intensive sectors because price signals were not allowed to adjust to reflect relative values. This in turn meant that a liquidation of this over-investment should have occurred during the downward part of the business cycle. However, this was not able to happen during the Great Depression due to other interventionalist policies which maintained and in some cases worsened the over-capitalization of long-term investment.

Barber 1985 gives a complete story of how this trend in economic thinking then lead to interventionalist administrations in the USA, from Coolidge to Hoover to Roosevelt. Part of this school of thought, and the presumed need for government interventionalism to make the best use of society's resources, was based on American economist/sociologist Thorstein Veblen's writings which described a dialectic in American society, one in which the engineers make the best use of productive resources and that these resources were not fully utilized due to the pecuniary interests of businessmen. *The Report of the President's Conference on Unemployment* (1921) also introduced the concept of "lifting power" (maintenance of aggregate demand) into the economic pantheon.[7] It was for these reasons then, when the stockmarket crash occurred in October 1929 due in part to a Fed monetary tightening after an expansionary 1920s, that President Hoover (who after all was known as the "Great Engineer") held a series of meetings at the White House to elicit industry's assistance in keeping wages high while reducing the number of hours per worker at the expense of increasing output. Prescott 1999 makes the case that it was this institutional interventionalism which kept unemployment high during the Great Depression because unemployed workers did not have the ability to compete down wages.

Many economists believed in the 1930s that an expansionist ("deficit spending") fiscal policy was necessary to increase economic activity during the period, not least because the fixed Gold Standard continued a contractionary monetary policy in the United States (Davis 1968, Parker

[7] Howenstine 1946 states the counter-cyclical "lifting power" of a predicted 1/3 reduction in the drop of aggregate demand for every one dollar increase in public works (as cited in the 1921 *Report*) became "scientifically streamlined as the 'multiplier'", page 481.

2007).[8] However, during the four years of the Hoover Administration (1929-1933) the Federal debt increased from 20% of the economy to over 40% of the economy (Carter et al 2006), yet unemployment increased drastically from 9% in 1930 to 25% in 1933 despite the fiscal expansionism. To reiterate what in hindsight was the futility of the attempted fiscal policy expansionism at the time, Romer 1992 states, "Fiscal policy, in contrast [to monetary policy], contributed almost nothing to the recovery before 1942", (page 781). It was only with World War Two production, and the abandonment of the government-encouraged cartelization and wage and price controls placed on the private economy during the 1930s, that employment returned to 'normal' (less than 5%).

Therefore at the time of our period of study for this paper on America's first concerted use of public works as 'employment stabilization' at the federal level, we had a contractionary monetary policy, a fruitless expansionary fiscal policy, and institutionalized constraints against wage competition and therefore factor rigidities which prevented a movement towards full employment.[9] It is no surprise then given these historical conditions that many economists were amenable to, and supportive of, employment stabilization programs which would allow the federal government to directly create jobs.

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[8] Parker 2007 cites examples from economists using the "Gold Standard Hypothesis" of the Depression that countries only began to recover after pulling out of the Gold Standard, the US in 1933.

[9] Schumpeter in his 1930 presidential address to the American Economic Association stated that depressions were inevitable and that factor rigidities were partly to blame for the current unemployment levels, "Everywhere wages are higher than is compatible with full employment", quoted in Dorfman 1959, page 661.

The State of Play in Economic Thinking in the 1920s

In general using the *reductio ad absurdum* mode of explication we can outline two opposing 'schools' of economic thought; that of *laissez faire* (or the free-market) and that of government interventionalism. It is clear that when a nation is at war, and therefore some of a nation's productive capacity is used to fight that war, that a given economic environment is not one of *laissez faire*.[10] This state of interventionalism is what the USA found itself in at the end of World War One.[11] We can classify economic interventionalism into three categories; monetary policy, fiscal policy and rule of law (an interventionalist rule of law is regulatory or institutional interventionalism which goes beyond that of negative rights[12]). We shall now explore each of these interventionalisms and their state of play in the 1920s.

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[10] In fact Cameron and Neal 2003 make the argument that there has always been a ruling class since the beginning of recorded history, and thus governments which extract resources from people involuntarily. Therefore again using the *reductio ad absurdum* logic of reasoning, there has never been *laissez faire*, there has only been varying degrees of interventionalism, with of course some exceptions, see Marx 2000.

[11] The War Finance Corporation founded in 1918 (and not abolished until 1939 by which time the Reconstruction Finance Corporation had been established) was used to provide subsidies to US farmers, especially after the retaliations due to the Smoot-Hawley tariff of 1930 caused US farm product exports to drop 30% by 1933 (Parker 2007).

[12] The concept of negative and positive rights is most commonly attributed to philosopher Isiaih Berlin, see for example, "Two Concepts of Liberty" in Berlin 1998. Negative rights are a rule of law regime where all citizens are treated equally. Positive rights are when some groups have preferential treatment over others under the rule of law. Preferential treatment under rule of law is allowed by the US Constitution under which the federal government is given the right to negotiate trade treaties, these treaties since the founding of the republic have given preferential trade treatment to certain, changing depending on the political climate, classifications of goods, protecting the

The most obvious example of economic interventionalism in the 1920s is the Federal Reserve System, created in 1913 to give monopoly power to a single institution for monetary policy in the United States.[13] The most common reasons given for a centralized monetary policy was to prevent financial crisis, especially against the cyclical necessities of the American agriculture sector whose needs were not being met under the haphazard American system of unit banking and state-by-state regulation of banking.[14] Therefore when it was seen that the central bank helped to countenance the Depression of 1920-21, it became accepted for economists to call for the Federal Reserve to pursue price stability. The most prominent economist calling for this policy of price stability was Yale University's Irving Fisher who stated, rightly or wrongly, in

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producers of these goods from foreign competition. In addition the interstate commerce clause of the constitution is often evoked to give the US government statutory authority to intervene in the economy. It should be noted that some contemporary economists believe that rule of law issues should not even be considered as part of the field of macroeconomics, see, i.e., Taylor 2004.

[13] The hegemony of a single central bank in the 1920s should not be overstated. Under the founding ideals of American federalism and perhaps too those of American pragmatism as practiced, the central bank's 12 regional offices, until the Roosevelt Administration's reforms cumulated in the Banking Act of 1935, had certain degrees of freedom to set monetary policy regionally. It is argued in Gaddis 2005 that Hoover supported this decentralization in monetary policy, and in fact supported a 'leadership' or 'coordination' role (as opposed to 'control' or 'mandate' role) for the US President in economic policy-making. This is confirmed with the voluntary nature ("moral-suasion") of Hoover's experiment with a federal public works program as shown in this paper and Hoover's 1930 White House conferences on wages stabilization which were indeed labeled as 'volunteered' by industry at the time. Under Roosevelt and the National Industrial Recovery Act and the Wagner Acts, these volunteerist wage stabilization policies were sweetened by guaranteed monopoly rents through higher prices for outputs, on condition that the rents be shared with the labor unions.

[14] See Smith 1934 for a history of U.S. banking policy from the founding up to the creation of Federal Reserve in 1913.

1926 that the “evils of farmers”, who were faced with lower market prices because of increasing competition and increasing productivity in farm outputs in potential export markets as Europe recovered from the war, was due to “leftovers of the deflation of 1919 and 1920” (Barber 1985, 26).

There were of course exceptions to the consensus that monetary policy be left to the Fed or that the Fed policy of price stability was indeed counter-cyclical or good for long-term growth. Charles E. Persons, writing in 1930 on the 1920-1929 period, believed that price stability led to an over-extension of credit (Persons 1930). On the other end of the spectrum, John Commons believed that the Fed was not able to created enough liquidity and in 1931, “proposed issuance of greenbacks for federal salaries, government debts, unemployment relief and for refinancing of farm mortgages until attainment of the 1926 price level” (Reeve 1948, 28). Ludwig von Mises and Frederich von Hayek both were contemporarily critical of the Fed’s expansionist-stabilizationalist policies and believed they lead to an unsustainable boom in the 1920s. However White 2008 makes the case that the Austrians were ignored, or in fact un-read, by American monetary policy-makers.

Fiscal policy was a different story. Except in times of war the federal government of the United States did not run budget deficits, fiscal policy was not seen as a tool of economic management, merely a necessary means by which to fund government (in fact the US Government itself was less than 5% of the US economy before World War One, it was not until after the New Deal and World War Two that the federal government reached its current approximately 40% of the economy. Fiscal policy was just not that *important* economically in the 1920s). The use of

fiscal policy to 'stimulate' or 'stabilize' the economy did not become accepted economic doctrine until the wide-spread adoption of Keynesian economics after the 1930s, although as well shall see later, by the early 1930s economists were calling for the use of fiscal policy to 'stabilize' the economy.

We can view fiscal policy in the United States during the 1920s as an embodiment of Andrew Mellon[15] who served as Secretary of the Treasury from 1921 to 1932, through four different Presidents, "From his perspective, the central priorities of fiscal policy were expenditure containment, debt retirement, and tax reduction" (Barber 1985, 54). In fact if anything a 'supply-side' approach to economic thinking where fiscal policy is concerned seems to have been the accepted doctrine. Tax cuts led to more revenue for the government. "No explicit, comprehensive theory of national income determination went with this idea about revenue-raising tax reduction, which is not to deny that one could be constructed. But reductions in federal income taxes in 1924, 1926, and 1928 were each followed by an increase in federal revenue. To some, this seemed proof enough that a tax cut would or could raise the national income and thereby raise the revenue" (Stein 1966, 192-193). Another reason can be given for an implicit regime of balanced budgets during peace-time, "Deficits at the federal level were also dubious for another reason: there was always suspicion that that they might be covered through the irresponsible creation of new money, a financing device not available to state and local governments" (Barber 1985, 20).

[15] The main reason Hoover was confirmed as commerce secretary by the Republican Senate in 1921 was on condition that Mellon be appointed treasury secretary by President Harding (Stein 1966, 190).

At the risk of generalizing a complex subject, itself worthy of entire monographs, it might be safe to say the normative aspects of American institutionalism in economics were entrenched in the American culture in the 1920s. There did not seem to be an adherence to a neutral, *laissez faire*, rule of law in the minds, and policy recommendations, of American economists, as there was, say, in the English school of economics. A.W. Coats 1960 makes the case that the American Economic Association itself was founded by those most interested in social reform. The esteemed American economist J.M. Clark[16] wrote two treatise in the 1920s dealing specifically with normative institutionalism, *Studies in the Economics of Overhead Costs* (where he applied value theory to the worker and stated that labor was not merely an input factor to be dealt with using the marginal productivity theory for costs of production) and *Social Control of Business* (which called for government regulation of business to maximize social welfare). Joseph Dorfman in *The Economic Mind in American Civilization* lists the changes in American economic life since the time of the marginal revolution as outlined in Clark's two treatises.

> Most of the changes occurred since 1873 and have continued at an accelerated pace. There has been the growth of effective control of railways and public utilities. Electrical power and the telephone have developed, first into recognized public utilities, and second which transcend state boundaries, and thus become essentially national problems. In this area falls irrigation, land reclamation and flood prevention, while radio and aerial navigation have only recently been added to this list. Anti-trust laws and the Federal Reserve system; vast developments in labor legislation, such as social insurance, minimum wage laws, and the compulsory arbitration of industrial disputes; pure food laws and the growing control over markets and marketing; enlarged control over immigration and international trade; urbanization with city planning and zoning; all have come about within this period. For the near future he envisioned such measures as health

[16] In 1935 Clark wrote *Economics of Planning Public Works* for the National Resources Planning Board, which was created under the Employment Stabilization Act of 1931. The Act of 1931 was the only time Hoover was able to gain official Congressional approval for the federal coordination of public works.

> insurance, control of the business cycle and unemployment, and the insertation of social control within the structure of industry itself through the "democratization of business" (Dorfman 1959, 455).

Economic thought and practice in the 1920s is the beginning a "new" economics. The economist is no longer seen as an avatar of the free-market and a seeker of economic efficiency. Social considerations are taken into account, especially those relating to the costs of industrialization, wage labor and the growth of cities. The central bank is used as a countercyclical tool and rule of law is extended into social (government) control of business. In the next section we shall focus on the use of government spending on public works programs as a means to "stabilize" employment.[17]

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[17] It may be overstating the obvious that a free-market economist would point out, as the Schumpeter quote above highlights, that economic downturns are inevitable and perhaps it is the very interventions of economic stabilization for *output and investment* in the first place which then require *more* stabilization policies for *employment*. The concept of one intervention necessitating another is known as "Mises' Law".

It should be noted here too, as is not part of the interventionalist measures mentioned above, that there was not yet consensus as to whether or not the management of 'normal' business cycles was a government (as opposed to central bank) role. "Business cycles are the unavoidable results of human nature. Depressions in moderation undoubtedly serve a useful purpose. They lead to economy, to thrift, and to the prevention of waste; but carried to the extreme they became disasters of the first magnitude. Every effort should, therefore, be made to prevent the intensity of great depressions such as occurred in 1873, 1893, and in 1929" (Harriman 1932, 74). Also for example a 1922 bill introduced in Congress promoted by the National Unemployment League was to authorize appropriations to secure "employment for all workers in times of business depression, through the establishment of public works by federal state and municipal government". This bill (which failed as did all attempts at creating a Congressionally-authorized national public works policy until 1931) specifically "did not establish a policy of

The Genesis of the "Hoover Plan"

The key person in the development of American policy for public works is Otto T. Mallery, a member of Pennsylvania's State Industrial Board and secretary of the state's Emergency Works Commission. Like Hoover, Mallery was an engineer, and therefore a man of his time when it was seen that engineers were the source of wealth-creation. Economics too, with the mainstream acceptance and use of General Equilibrium Theory, viewed the economy as a closed engineering-like construct. If we look at Figures 1 and 2, both taken from the *Report of the President's Conference on Unemployment* (1921) and of which Mallery was instrumental in writing under Hoover's chairmanship, we can see the convergence of these concepts. In Figure 1 we can see that the economy is modeled as a closed system, resembling a system of interconnected water lines.[18] When needed for "pump-priming", public works can be 'signaled' (the water main turned on) which then triggers the necessary increase of pressure in the system, creating economic activity and jobs, at each submain we see the flowthrough as creating "added employment wages". In Figure 2 we see through the elongated lever on the left-hand side that there is a multiplier effect, greater than the sum of expenditures from "concentrated public works construction" which has an effect on "industrial activity and employment". Mallery visualized

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timing public works to compensate for the ups and downs of the business system" (Howenstine 1946, 487). It is clear that the concept of timing of public works to be countercyclical was not universally accepted as either effective nor necessary, although the efficiency aspects (of not crowding-out private spending during the upswing and taking advantage of lower costs during the downswing) does appear to be the most commonly-accepted economic argument for any central coordination of public works.

[18] Figures 1 and 2 are copied from Barber 1985, pages 17-18.

these trickle down or multiplier effects like a pebble "rippling" though a pond Barber (1985, 18). Public works is presented as way to create jobs and "extra demand".

Macroeconomics, let alone an interventionalist fiscal policy as a subdiscipline, was not yet formalized in the 1920s, whereas of course public finance had always been a part of economics, due to the necessity of funding government. Therefore we might find in the 1921 Conference on Unemployment the beginnings of fiscal policy as a field in economics.[19] The Conference itself held several committees, the one on public works was headed by Mallery and underneath Mallery's Public Works Committee was the Economic Advisory Committee (Howenstine 1946). For our purposes here we can note that economics was seen as supportive of, not a driver of, public works policy. Public works spending itself was seen as the tool for aggregate demand creation. Aggregate demand was not to be created by a generic "fiscal stimulus" of which public works was only one part. Public works spending was seen as the countercyclical demand creation, with economics, in this case public finance, seen as a support mechanism for the public works.

[19] The 1921 Conference might also be seen as the beginning of business cycles research in the USA (Mises had already written in German about cycles in 1912's *The Theory of Money and Credit*), which resulted in the 1923 *Business Cycles and Unemployment*. The first comprehensive macroeconomic statistics in the US, the *Survey of Current Business* (1921, now published quarterly by the US Department of Commerce) was also the result of the 1921 Conference. W.C. Mitchell's National Bureau for Economic Research had been founded a year earlier and received a large grant from the Conference to study business cycles and public works alternatives.

In the published findings of the Conference we can discover the nascent field of fiscal policy and see how public works policy was viewed as something separate from fiscal policy at the time.[20] Although most of the recommendations were not passed into law at the time, they did form the basis for what later would be known as the "Hoover Plan" for a public works policy at the beginning of the Great Depression. In the first instance, public works were something which was to be *planned* (for this a National Planning Commission was recommended, this was not approved by Congress until 1931). Federal government public works expenditures represented around 10% of these expenditures, with state, county and municipalities representing around 90% of public works historically.[21] In the 1921 *Report* the planning of public works was seen to be a countercyclical (preventative) measure against unemployment, not an after-the-fact relief measure, and the arguments for public works at the time stressed the efficiency of central planning for public works, not the humanitarian relief aspects.

By timing government public works expenditures - at all levels of government – efficiency in spending could be achieved. If the spending was timed to occur right at the beginning of the downward portion of the business cycle then factor inputs would be less expensive than if they were not planned and had to compete with private construction. This planning then was to

[20] Mallery also published *The Long-Range Planning for Public Works* in 1923, available through the NBER, http://www.nber.org/chapters/c4671

[21] These ratios held throughout the period 1921 through 1928 until the Hoover administration public works expenditures (Barber 1985). It was only beginning in the Roosevelt Administration that federal expenditures, both for public works and for all government expenditures in the economy, exceeded state and local expenditures (Weber 2008).

prevent public spending from "crowding-out" the private use of construction resources during the upward part of the business cycle and at the same time reduce the costs of the public expenditures on public works as they were timed during the downward portion. This type of planning requires the use of large amounts of statistical information and it is for this reason that the Conference was able to put into place the on-going *Survey of Current Business* published by the Department of Commerce beginning in 1921. In addition the Commerce Department, in conjunction with the American Construction Council (headed by Franklin D. Roosevelt), published the *Seasonal Operation in the Construction Industries* in 1924.[22]

The second issue of consequence addressed by the 1921 Conference was the *financing* of public works. The timing of works was one thing whereas the funding of public works was something else. The Keynesian idea of deficit spending as a stimulus during the bad times and the reduction of the debt during the good times, as we have seen, was not yet part of a practicable fiscal policy.[23] The funding for public works then had to be something separate from

[22] The Public Works Committee found that, "Custom, not climate, is mainly responsible for seasonal idleness in the construction industries. Contrary to popular belief, bad weather is not the principal cause of variations in employment from month to month" (Howenstine 1946, 485). The American Construction Council then may have cooperated with the production of the report as part of an "educational outreach" program in order to prevent further regulation.

[23] Depending on the value judgments of the reader, the use of Keynesian economics through today since the end of the Second World War may seem impracticable as well due to the fact that unlike the weather an increase in government debt can be counted on except for exceedingly rare off-years.

Congressional appropriations.[24] "No one demanded, or as a practical matter, expected, that it [public works] would be financed out of current taxation" (Stein 1966, 194).

There were four main avenues for public works funding under discussion at the time. The first two dealt with the non-federal entities (who managed 90% of the public monies spent on public works). The most commonly discussed method for financing works when needed for countercyclical stimulus was that of sinking funds or set-asides, where it was recommended to state and local governments and to public utilities that they set aside a certain portion of their annual budgets to save public works monies for a rainy day, "for a rough calculation indicates that if we maintain a reserve of about 10 percent of our annual construction for this purpose, we could almost iron out the fluctuations in employment" (1921 *Report*, 160). The concept of a sinking fund, like that proposed to the states, was already part of the US government budgeting protocol, but it was reserved for the retirement of debt accumulated during the war and was classified as normal expenditures, something which a central-planning of public works to act in a countercyclical manner was not intended to be (Barber 1985, 20). The Report also recommended that municipalities "float bond issues in order to expand their construction programs" (Reeve 1943, 208) as an immediate counter-measure to unemployment. It was the special bond issues which became the more useful in practice.

[24] The Harding administration attempted throughout the 1920s to gain Congressional appropriations for public works, these attempts all failed under a Republican Congress.

On the federal side (10% of public works spending) the two main financing mechanisms under discussion were special bond issues and the direct raising of funds from the general public through a Liberty Bond concept, like the funds-raising "buy-in" efforts used to help finance the first World War. *Business Cycles and Unemployment* (1923), the result of follow-on work funded by the 1921 Conference on Unemployment (and drafted mainly by Mallery) recommended that a Public Works Reserve Fund be created.[25] This fund would consist of pre-authorized bond issues, government-backed bonds used to fund public works, which in turn were matched by a pipeline of public works at the federal, state and local levels and which would "anticipate needs of the near future when unemployment is the greatest" (Howenstine 1946, 484). The Prosperity Bond idea to fund public works, like the Liberty Fund bonds used to fund war, first was floated in an editorial in *Engineering and Contracting* magazine in 1921, and became part of the debate throughout the period of over 'employment stabilization'.[26]

[25] Mallery also recommended the creation of a cabinet level public works department, this as of yet has not been created in the USA. Neither Coolidge nor Hoover attempted this, Roosevelt attempted twice. The nearest thing to a public works ministry in the USA is the Department of Transportation, established in 1966. It should be noted that economist William Leiserson had perhaps the most radical call for employment stabilization in the period, suggesting that a Federal Labor Reserve Board be established "to do for the labor market what the Federal Reserve Board did for the banking interests" (Howenstine 1946, 483, original source the 1921 *Report*). Bert Ely in 1931's *Hard Times: The Way in and the Way Out*, recommended a similar approach, a peacetime army which would absorb the unemployed and put them to work in government public works projects, this "became the Civilian Conservation Corps of the New Deal" (Dorfman 1959, 671).

[26] The Prosperity Bond concept was eventually endorsed in 1930 as the Prosperity Loan by the mayors of 58 cities and 90 "leading economists" (Reeve 1943 , 8) as a $1 Billion Treasury bond floatation to be sold directly to the people. We can see this concept of extraordinary spending being taken directly to the voter in today's discussion over the Obama Bonds or Bailout Bonds to finance the government's interventionalism in the financial markets.

The groundwork was laid for an activist fiscal policy through public works, something which both captured the "new economics" of stabilization and the new concern over social policy for the unemployed. However, political realities prevented the adaption of a federal works policy, either for efficiency reasons or for countercyclical reasons, "…much of the footdragging by politicians stemmed from their reluctance to cede spending powers of government to experts and to formulas....it will not get votes." (Barber 1985, 23).

The Road to Works, Part One

Despite the ineffectiveness of Hoover and Mallery to create enough special interest group agitation to enforce a Congressional approval for an institutionalized activist fiscal policy throughout the 1920s, the Conference on Unemployment of 1921 had begun to change economic thinking and action at a decentralized level.[27] The Conference of 1921 had an immediate impact

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Today's situation however is directly related to a more coherent fiscal policy regime (and where the size of government is much substantial than it was in the 1920s and where the US is a debtor nation instead of a creditor nation) where it is seen in international debt markets that the US deficit spending may not be sustainable, nor the dollar's value assured, given the federal government's annual budget deficit's rapid increase during the last G.W. Bush administration, the proposed Obama administration's spending plans, and the rapid increase in Fed liabilities to finance the bailouts.

[27] A spate of economists interested in specialized fields used the concept of public works policy in their research in the 1920s, here is a selection from Dorfman 1959: Leo Wolfman, labor economist, supported subsidies to railways as employment-generating; J.M. Clark, social economist, stated government works should be 'elastic' in implementation and planned far enough in advance ("shovel-ready" in today's vernacular) in order to take effect during times of depression; Isador Lubin, labor economist, believed government should coordinate public works but

at the state and local levels where by the end of 1921 bond issues for public works increased dramatically and were at their highest level on record (Barber 1985, 23).

In addition Hoover himself began to use his position of influence within the government to implement the ideas of public works as a countercyclical measure. In 1921 Hoover as Commerce Secretary, in order to convince the nation's mayors of his devotion to a countercyclical public works policy, convinced President Harding to "speed-up" government spending on public works. Then, as the nation began to recover from the 1920-21 recession (actually it had recovered but there are always lag times in the knowledge of such things), Hoover in 1923 pressed for a "slowdown" of federal works projects in order to prevent 'crowding out' private spending during the upswing, stating, "We can by this means contribute something to a more even flow of employment not only directly in the construction work but in the material trades" (Howenstine 1946, 488). This 1923 action was supported by both the American Construction Council (headed by Franklin D. Roosevelt and Irving Fisher, the latter who said, "While we students have been discussing how to it [stabilization], Mr. Hoover, Franklin Roosevelt, and the bankers have been doing it" (Dorfman 1959, 50n).

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that works were not a 'cure-all', especially if were subsides to 'problem' industries, and; Frank G. Dickinson, economic historian, used the multiplier theory from the 1921 *Report* to estimate how a 'perfectly' timed program of public works would have alleviated the effects of the 1920-21 downturn.

The End of the Road

We now pick-up (and end) our story where we began, with the Great Depression. For all intents and purposes, there was no perceived need for any countercyclical or unemployment interventionalism after the end of the 1920-21 period up until the Great Crash of 1929. This of course may help to explain why public works were not institutionalized into American policy-making during the 1920s except for the relative minor end-round by Hoover from 1921 to 1923 after the initial enthusiasm generated by the 1921 Conference on Unemployment.

The stock market crashed in October 1929 and in November now President Hoover began asking public utilities, states and municipalities to spend on their "shovel ready" projects immediately and to report estimated outlays for 1930, just as the 1921 Conference on Unemployment recommended and as practiced in 1921 to 1923. William J. Barber writes of this Presidential activism that, "Never before had the nation witnessed presidential activism on such a scale during a period of economic disturbance" (Barber 1985, 82) and shows that spending increased in 'regulated industries' by an average of around 5% from 1929 to 1930 and a full 20% in the public sector (page 93).

However by the time 1930 became 1931 it became clear that the high-wage doctrine, the decrease in trade brought by the Smoot-Hawley tariffs, and the contractionary Gold Standard were preventing a recovery (although these reasons did not become clear until many years later). In addition it was seen, at the time, that further public works expenditures would not be fruitful,

there just weren't that many shovel-ready projects after the 1929-1930 expenditures. Furthermore Hoover's hands were tied fiscally, preventing further federal public works expenditures. The early payout to World War One veterans[28] and the rapid depletion of government revenues due to both the failing price levels and the contraction in output in 1930 and 1931 lead to the largest peacetime budget deficit as a percentage of the economy in the history of the United States. In December 1930 Hoover's newly created Emergency Committee for Federal Works tried to gain lobbying support for a $1 Billion Prosperity Bond but this was not approved by Congress; it was viewed that the "public works" stimulus of 1930 did not work. Hoover just was not able to pursue an expanded public works program during the Great Depression, despite what by then was an ideal strongly supported by many economists. [29] It would take President Franklin D. Roosevelt's Works Progress Administration and a vastly enlarged federal government - the welfare state - before an active fiscal policy, to include public works, became accepted policy in the United States.

[28] The Bonus Bill of 1931 represented 3% of person national income (Barber 1985, 110).

[29] The economics profession had institutionalized the tools of fiscal policy: the 100th edition of *Survey of Current Business*, began with the 1921 Conference on Unemployment, would be published in December 1929, the National Bureau for Economic Research was firmly established and the study of business cycles as subfield of economics was gaining momentum.

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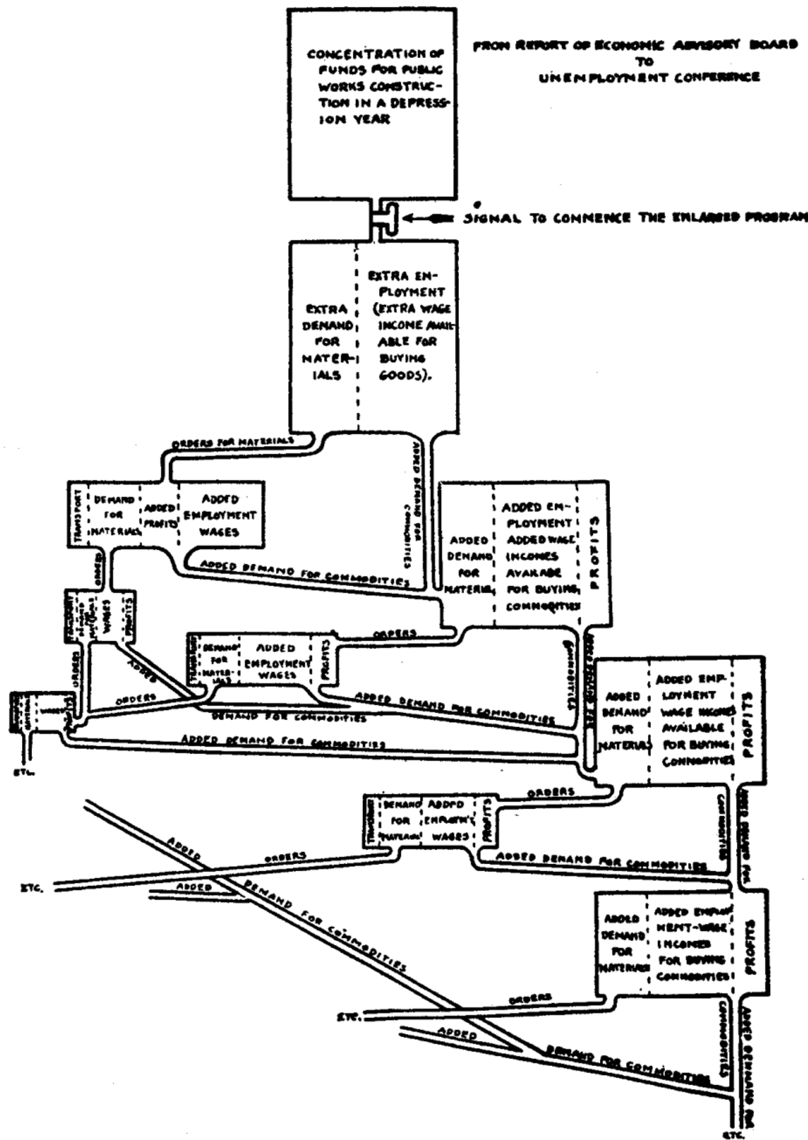

Figure 1. Aggregate stimulus to private industry caused by pressure of concentration of public works construction in depression years. Reprinted from *Report of the President's Conference on Unemployment*, 1921, p. 102.

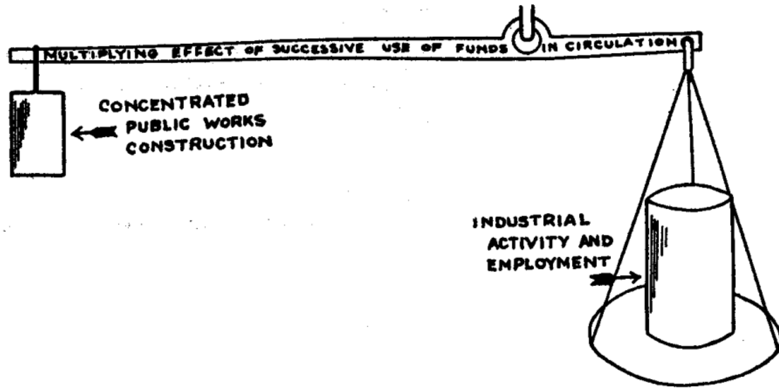

Figure 2. Manifold power of concentrated public works construction to sustain and revive industry. Reprinted from *Report of the President's Conference on Unemployment*, 1921, p. 103.